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Robert Hiester Montgomery (1872-1953)

Harvey S. (Harvey Stuart) Chase (1861-1946)

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THE REPORT OF THE PRESIDENT'S
COMMISSION ON BUDGET CONCEPTS

Robert M. Trueblood
Federal Government Accountants
Association
Washington, D.C.
January 11, 1968

It is gratifying to be called upon to meet with fellow accountants to discuss a matter of considerable social importance to this country -- and a matter that has special implications for those of us who practice accountancy. My pleasure is not diminished by the thought that inviting an accountant to Washington is an event on the order of piping gas to Texas.

This is the city where great undertakings -- the most extensive and the most expensive ever devised -- have their origin. This is the city where decisions are made as to how our vast public resources will be used to accomplish far-reaching public objectives.

Those decisions center, to a large extent, on the President's proposals made each January to the Congress -- proposals embodied in that remarkable document -- the United States Budget. This budget is perhaps one of the most baffling, hard to use, and hard to understand documents of its type.

In recent years, the United States budget has been showing signs of age, and the effects of a hard life. Created initially by the Budgeting and Accounting Act of 1921, the budget has changed continuously since that time. The President has almost complete flexibility in his budget presentation. Budget changes -- year by year -- are initiated by the President himself, or by the Budget Bureau, or by the Congress. These changes are made

in response to social or economic pressures, or simply in order to remedy some problems in the nation's bookkeeping.

Within a few years after the 1921 Budgeting and Accounting Act, the budget entered on hard times along with the rest of the country. During the Depression, Congress and the President -- desiring quick action on relief and recovery -- bypassed the orderly budget processes and put large sums of money to work without prior or detailed itemization. Emergency appropriations were made throughout the year, whenever the need was expressed. The concept arose of two budgets -- one for the regular operations of government, and the other for emergency operations.

The varying ideas of what a budget should be -- or what budgets should be -- were not confined to those generated by the problems of the Depression. Rather, the social and economic environment of the country continued to change; new budgetary ideas continued to be advanced; and budget concepts continued to be adjusted throughout the war and postwar period, up to the present time.

Finally, today there has emerged a set of competing concepts -- each purporting to be "the" budget, and at varying times each being "the" budget. The most important of these competing concepts are the administrative budget, the consolidated cash budget, and the national income accounts. Each budget or tabulation

serves a different purpose, and so the convenient argument has emerged that no one budget can fulfill all the purposes of a federal budget. That is an interesting argument, worth a few moments of our time -- and we will return to it shortly.

But the budget, over time, has become all things to all people. It is a multiple budget, with its segments built on contradictory concepts -- hard to reconcile, hard to understand, and hard to work with. Different budget concepts have, in fact, competed for attention, each telling a different story.

Hence, ten months ago, President Johnson appointed a 16-man commission to examine the Federal Budget, and to recommend ways to make it more

understandable and useful for public planning and for social decision-making.

David Kennedy, a leading American banker, was named chair man of the group -- a group which also included the chairmen and ranking minority members of the Senate and House Appropriations Committees, Secretary of the Treasury Fowler, Budget Director Schultze, Comptroller General Staats -- and others from finance and academia.

The Commission was given a broad charter ... to undertake a thorough review of the budget, and to recommend an approach that would make the budget more intelligible to both the public and Congress.

Rather, the Commission addressed itself to the conceptual problems of what the budget ought to be, and to what the budget ought to do. The Commission rightly concerned itself in establishing and recommending criteria and rules by which the budget could be made a more understandable document, and a more useful instrument for public policy decisions -- now and in the future.

After a six-month study, and we all wish there had been more time, the Commission made its recommendations last October. Less than a month ago, as you undoubtedly know, the President approved the Commission's report and its recommendations for adoption in the budget for fiscal 1969.

The full recommendations of the Commission are covered in its report of some 100 pages, which I'm sure many of you have read. Staff papers and other materials reviewed by the Commission will be published as a companion document shortly. My purpose this evening is not to go into the details of the report. My purpose, rather, is to summarize the important recommendations in that report. And I want to spend a little time later on several topics of considerable interest to us as accountants and managers -- which were not fully treated by the Commission.

* * * *

Before discussing the nature of the Commission's recommendations ... and their implications ...

let me go back to that argument to which I referred earlier -- that no one budget can perform all the jobs that a budget must or ought to perform.

And what are some of those jobs? The budget, in its direct effect, supports the maintenance and provides for the alteration of government operations. But the budget has far-reaching implications for the public at large, for business and for labor, for finance, for our international relations, and for a host of other groups, persons, and institutions.

Some of the more specific purposes of the budget are these:

- ... It requests funds from Congress for on-going programs and for new programs, and it requests changes in the revenue system.
- ... The budget proposes an allocation of resources as between the private and public sectors of the economy in order to serve the national purpose.
- ... The budget is the basis for national income analysis.
- ... It expresses the economic and social policies of government with relation to the maintenance of high employment, price stability, economic growth, and balance-of-payments equilibrium.

- ... Figures included in the budget measure the size of government.
- ... The budget document provides information essential to the Treasury's management of cash resources and the public debt.
- ... It provides information useful to business, the farmer, and the working man; and it is an accounting, to all citizens, of the government's stewardship of public monies.
- ... Finally, the budget provides a basis for analysis of the impact of the government on the money market.

No doubt, these and many others are important purposes for a budget. But can all of those purposes be fulfilled by a single document? For some years this task has been divided among three budgets -- and many ancillary calculations:

... The administrative budget provides a measurement of government programs and their cost, but it excludes the activities of funds -- such as the social security and highway trust funds -- and other earmarked accounts.

... The consolidated cash budget is most useful for cash flow analysis, but it is not a good measure for many government programs.

... The national income accounts are concerned primarily with economic analysis.

These three measurements of government financial activity are competing. These three measures can be used together ... as the Commission noted ... "only with a fairly elaborate reconciliation that tends to confuse more than it enlightens."

The Commission quickly decided that any one of the present budgets could not satisfy all requirements. Commission members also agreed that a single unified budget was the most important recommendation that the Commission could make. To determine the shape of that unified budget, the Commission decided that the two most important purposes of the budget are:

1st To propose particular military and civilian programs designed to promote

national security, international cooperation, and domestic progress.

And 2nd To propose total expenditures and revenues designed to permit the government to fulfill its obligations to maintain stable economic prosperity and growth.

In the words of the report, "The budget must serve simultaneously as an aid in decisions about both the efficient allocation of resources amongst competing claims, and economic stabilization and growth."

The Commission's most important recommendation by far is for a unified budget, which provides for both of these purposes within a single conceptual and structural framework. The Commission recommends that the administrative, cash consolidated, and NIA budgets

should be no more. The information they contain may continue to be provided within the budget document, together with all other useful information. But there should be only one document or tabulation known as The Budget of the United States, and that document should be prepared on the basis of concepts adopted by the Commission.

I want to make it clear that the Commission's recommended budget is really a broad financial plan for the government. I think this very important perspective of the Commission's proposal has unfortunately been obscured in press reports and interviews.

The Commission's proposed financial plan consists of four parts:

- 1st Congressional appropriations;
- 2nd Receipts, expenditures, and net lending;
- 3rd The means of financing the budget deficit
(or disposing of a surplus); and
- finally Information concerning federal borrowing
and lending programs.

Incorporated into this financial plan format are a number of other significant recommendations upon which I will comment only briefly:

... Part I of the recommended financial plan consists of a summary of appropriations requested from the Congress. The purpose of this deliberately primary placement is to emphasize the difference between

appropriations and expenditures.

As you accountants in the federal establishment realize, an expenditure made in one year may come from an appropriation of that year, or of previous years. Conversely, an appropriation legislated in one year may become an expenditure in that year, or in subsequent years. Highlighting appropriations, the Commission feels, will eliminate a good deal of the confusion resulting from the difference between appropriations and expenditures.

... Part II of the recommended budget ...
receipts, expenditures, and net lending ...
is most like the budgets currently in use.

This section of the financial plan will cover all government projects, including trust funds and lending programs. In order to facilitate economic analysis, however, the Commission has provided for a subtotal representing the difference between expenditures and receipts, not including lending programs. The Commission was quite emphatic, however, that only the net difference between receipts and expenditures including lending programs, shall be called the budget surplus or deficit. The subtotal for expenditures and receipts, excluding lending programs, is shown merely for analytic purposes. (As a side note, I might mention

that the treatment of lending programs was probably the most difficult problem with which the Commission had to deal.)

... The means of financing the budget deficit, (or the means of disposing of the budget surplus) is Part III of the recommended financial plan. Most importantly, in this section, the sale of participation certificates is to be treated as public debt, and as a means of financing. As you all know, PCs have been treated as negative expenditures in the budget, thereby reducing total expenditures and the deficit. The Commission's recommendation to regard PCs as a means of financing was the only

point on which there was a substantive dissent taken by any of the Commission members. Several members felt -- that at least to the extent to which PCs finance the lending programs -- PCs should continue to be treated as negative expenditures but the minority view on this point did not prevail.

... Part IV of the budget summarizes the outstanding amount of federal debt as of the year-end -- as well as the outstanding volume of federal credit, both direct and guaranteed. This section of the plan points out the great importance today of the federal lending programs, and particularly of the federal

guaranteed loan programs. Several Commission members argued quite persuasively for the inclusion of the guaranteed loans directly in the budget itself. However, since guaranteed loan programs do not initially or necessarily involve federal expenditures, the Commission decided to continue to treat such loans outside of the budget totals. (I will have more to say later, in generality, on federal lending and borrowing programs.)

* * * *

The Commission made several other recommendations which I think are of interest to many of you. These recommendations are not reflected, as such, in the

recommended unified budget structure. But they will manifest themselves in other ways during the budget presentation cycle.

Probably of major interest to you as accountants is the recommendation that the budget be prepared on an accrual basis. As you all know, the administrative budget is presently on a checks-issued basis; the consolidated cash budget is on a checks-cashed basis; and the NIA budget is prepared on a combination of accruals and deliveries. Speaking of the deliveries method of accounting, it has never ceased to amaze me that the NIA accounts record the cost of an aircraft carrier only when the carrier has been delivered to the Navy -- no matter how many years may have been involved in its construction.

Neither the checks-issued nor the checks-cashed nor the deliveries basis -- represents an accurate measure of the economic impact of an expenditure on the economy. By contrast, use of the accrual method would have allowed economists and others properly to assess the effects of the military build-up during 1965 and 1966. As it then was, the effects of Vietnam expenditures were not observed publicly until well after the fact. Another benefit of the accrual method is to encourage governmental agencies to use accrued cost concepts in their internal agency management.

The change-over to the accrual basis will not be easy. Even though the requirement for accrual accounting at the agency level was legislated in 1956,

several important governmental agencies are not in a position presently to regularly report accrued expenditures. Further, the Treasury has a good deal of work to do in researching better ways to estimate accrued receipts. However, the benefits for the agencies and for the nation make it very worthwhile in the Commission's view that both expenditures and receipts be recorded on an accrual basis.

I would like to comment briefly on some other recommendations of the Commission:

... In order to help promote a more efficient use of public resources, the subsidies involved in federal direct loan programs should be

separately identified in the budget document.

And these subsidies should be treated as a budget expenditure, not as a portion of the loan programs.

... Government receipts which are market-oriented in nature should be treated as negative expenditures, whether or not a revolving fund has been set up for such receipts. Perhaps the Commission's second most important point is that like items ... both receipts and expenditures ... should be treated consistently within the budget and from year to year -- without consideration of the legal niceties involved in enabling legislation.

... Budget information should be communicated to Congress and to the public with greater frequency, by providing within-year revisions of January estimates. Budget information should be provided in greater detail, by breaking down aggregate budget figures into quarterly or semi-annual units. And budget data should be more comprehensive, by provision of estimates which extend further into the future.

... A capital budget which treats capital or investment expenditures "below the line" should not be used in the United States. However, there is merit to analysis of capital expenditures and capital assets as part of the budget document.

* * *

I have spent some time in discussing the Commission's major recommendations and I have tried briefly to point out the rationale behind these recommendations. But before I close, I would like to spend some time talking about a few topics which were not, for good and sufficient reason, discussed at any length in Commission meetings or in the Commission's report.

* * *

As I mentioned before, the Commission was not charged with the responsibility, nor did it have the time, to investigate and recommend with respect to agency management techniques. At the individual agency level, however, budget preparation and agency management are closely inter-related. All of the

Commission's recommendations are compatible with, and will ultimately further, the use of effective management techniques at the agency levels. Moreover, the Commission did encourage and applaud the use of modern decision-making and control techniques by agencies.

Probably the most important of the new decision-making techniques is the concept of planning, programming, and budgeting systems which are now being implemented in most government agencies.

However, the key point to keep in mind about PPBS is that it is a planning technique only. It is a means to aid agency and government management in allocating funds amongst competing claims. PPB is not, nor does it purport to be, a technique to implement agency plans.

PPB requires that each agency state its goals, and define the most appropriate programs to carry out those goals. Each agency program is analyzed in order to ascertain its probable costs and benefits. Programs are then compared, one with another, to select those which offer the best cost-benefit ratio in order to accomplish the specified goals. Planning is projected on a five-year or longer basis, rather than on the more typical one-year budget review. As PPB becomes more effective, decision-making in the federal government will more and more be made on a comparative basis, and less on a subjective basis, than may have been the case in the past.

Probably the most difficult part of PPB is the definition of goals of an agency, or of a department. We as accountants can play an important role in that

goal definition. In addition, we as accountants, managers, and advisers must understand that typical accounting data are not sufficient for a meaningful PPB analysis. As goals are better defined, programs which have never before been performed will be actively considered. Accountants should help to develop and define new and better techniques to determine the cost of alternative programs and the benefits of those programs.

On the national level, PPB holds a great deal of promise for the efficient allocation of limited funds between departments. I think it will be some time before we can really do this in any meaningful way. We can, however, start to prepare now for the use of PPB concepts at the federal level by beginning to define the federal goal structure, and by providing a means whereby costs

and benefits can be aggregated consistently between, within, and across departments.

* * *

As I indicated previously, the Commission spent a fair amount of time discussing federal lending and borrowing programs. To tell the truth, I had not realized how closely the federal guaranty programs resembled direct loan programs, particularly in terms of economic impact. I was also impressed by the number of different agencies which can issue loans -- or which can guarantee loans at varying interest rates, for varying terms, and following various administrative practices. There also seems to be some justifiable concern within the governmental establishment that

the guaranteed loan programs are going to proliferate greatly over the next ten years. The concern is not that guaranteed loans are bad, and direct loans good -- or vice versa. Rather, the concern is that with the present lack of coordination between lending agencies, there may be a great imbalance between the guaranty and direct loan programs -- and, more importantly, no adequate overall coordination between the two.

By the same token, I was impressed with the number of federal agencies which can borrow funds from the public. Actions in the money market by one borrowing agency may appear to be at odds, I am told, with Treasury policy at any particular point in time. There apparently is no formal coordination between the

borrowing agencies which assures the best overall debt structure or the best overall fiscal policy for the federal government -- taken as a whole.

It seems to me that serious consideration should be given to new techniques to coordinate the various lending programs in order to achieve the most effective allocation of the aggregate resources of the economy. It seems to me that it would be appropriate for all borrowing by federal agencies to be coordinated officially -- in some manner. I do not pretend to know how either of these objectives may be best accomplished. I can look on my industrial experience, however, and point out that in all major corporations borrowing and financing are handled through one facility. Lending policies are made by a central group, even though the

physical acts of lending and servicing the loans may be performed at scattered physical locations.

* * * *

The last point that I want to touch upon is the concept of long-term projections. We all recognize that the social and economic environment today is undergoing extremely rapid change. The world five years from now will not look very much like the world today. In order to prepare for five years from now, we have to plan presently. In order to plan effectively for five years from now, we must be able to project costs, five years hence, of programs which are initiated today. Further, we would like to be able to project the costs

five years hence of programs which we are not going to begin until some years from now.

Most major corporations are recognizing the impact of change on their operations and are planning and projecting now for activities which will take place in the future. The pressures to plan change are just as strong for the government, as they are for the business community. In fact, such forces of change may even be stronger and more important in the case of the government. The first-year cost of any government program is typically like the tip of an iceberg. Most of the costs will be incurred in future years. Presumably, the larger benefits of government programs are also realized in future years.

Congress recognized the need for long-term projections when it decided that all new bills should include five-year estimates of cost. I understand, however, that this projection requirement is honored only in the breach. Further, I can well understand that most government agencies will not -- for reasons of politics and uncertainty -- attempt to define costs of programs which have not yet been initiated. I can well appreciate the reasons for resisting long-term projections for specific programs. I can be supportive of hesitancy with respect to making long-term estimates which are not necessarily related to existing programs. It was, in fact, for these reasons that the Commission suggested that an outside research organization be used to prepare five-year budget projections.

My only point is that such projections are indeed necessary and vital -- if the government is to initiate and manage changes in our environment. Such planning is also necessary in order to activate programs with long lead times in order to make them effective.

* * *

I think at this point I have talked quite enough for one evening. I feel that the sincere labor of the Commission was quickly rewarded by the President's far-sighted decision to adopt its recommendations -- even though the unified budget will show a larger expenditure total and a larger deficit in an election year.

According to Budget Director Schultze "virtually all of the basic changes which the Commission

recommended, and which can be feasibly undertaken in time, will be incorporated in the fiscal 1969 budget."

Basically, the only major recommendations of the Commission which cannot be implemented for fiscal 1969 relate to accruals and subsidies. Conversion to accrual accounting -- although long delayed -- will still require extensive preparation and major changes in significant portions of the government's accounting system. Studies for accomplishing this objective have begun, but it may be two years before the results can be reflected in the budget document.

The recommendation in regard to loan subsidies will also require further technical study and development.

Rome was not built in a day, nor an accounting system reformed overnight. But it appears that we will have a more useful and understandable budget document, as quickly as retooling can be accomplished.

The Commission has done its work. The President and the Budget Director have acted. I assume that the next step -- and perhaps the hardest work -- is up to you.

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